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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Application of AT&T Corp. And Teleport Communications Group, Inc. for Transfer of Control

ORIGINAL

CC Docket No. 98-24

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April 27, 1998

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**REPLY COMMENTS OF AT&T CORP.
AND TELEPORT COMMUNICATIONS GROUP INC.**

AT&T Corp. ("AT&T") and Teleport Communications Group Inc. ("TCG"), pursuant to Public Notices DA 98-369 (February 25, 1998) and DA 98-558 (March 24, 1998), submit these Reply Comments in support of their application for consent to the transfer of control to AT&T of licenses currently controlled by TCG.

INTRODUCTION AND SUMMARY

In an era in which telecommunications mergers routinely generate enormous controversy and opposition, only a handful of parties have even submitted comments on the application of AT&T and TCG. That is a reflection of the substantial public benefits that will be generated by the merger and the resulting transfer of control of TCG's licenses to AT&T. Most notably, combining TCG's decade of experience in breaking into entrenched monopoly local exchange and exchange access markets with AT&T's brand and marketing experience and efficiencies from the intensely competitive long distance business will produce a firm that will be a substantially more formidable local competitor than either TCG or AT&T could be alone. And, in contrast to other

recent telecommunications mergers that the Commission has approved, these enormous competitive benefits will not be offset by any substantial adverse effects in any market. That explains why the merger did not trigger a “second request” from the United States Department of Justice, and why it has already been approved by 17 of the 24 state commissions which will review it.

No commenter seriously disputes that the merger will enhance the competition that the Telecommunications Act of 1996 is designed to create. Instead, each makes unsupported allegations that the merger will cause harm in other respects. Under the Commission’s established merger standard (applied most recently in Memorandum Op. and Order, In the Application of NYNEX Corp. and Bell Atlantic for Consent to Transfer Control of NYNEX Corp and its Subsidiaries, FCC 97-286 (rel. Aug. 14, 1997) (“Bell Atlantic/NYNEX Merger Order”)), these allegations fall into three categories: horizontal allegations, vertical allegations and non-merger-related allegations. None has merit, and, at bottom, the comments merely confirm that this is patently a case in which “the merger will be pro-competitive” because the “benefits that enhance competition” are substantial and “outweigh[]” any possible “harms to competition.” Bell Atlantic/NYNEX Merger Order ¶ 2.

The combination of AT&T and TCG is predominantly a vertical integration, and the commenters accordingly offer little more than passing references to potential horizontal effects. By and large, the two companies simply do not today compete against one another for the same customers. There is virtually no overlap between the merging entities’ local or long distance facilities and services or with respect to the international or 38 GHz licenses that are the subjects

of the applications. And, even where minor overlaps exist, the market shares of one or both of the merging parties is so small that any resulting increase in concentration will be de minimus.

Nor does the vertical integration of AT&T's long distance business and TCG's local business raise any competitive concerns. Sprint and BellSouth worry that this vertical integration could harm them as competitors by reducing exchange access alternatives (in the case of Sprint) or access revenues (in the case of BellSouth). The proper focus, however, is on potential harm to competition, not to particular competitors, and, as the Commission has held, "[v]ertical effects that harm competition generally depend on the vertically integrated firm possessing market power in an upstream 'input' market and taking actions in that input market that leverage this market power in the downstream 'end-user' market." Memorandum Op. and Order, In the Matter of the Merger of MCI Communications Corp. and British Telecomms., FCC 97-302 ¶ 154 (rel. Sept. 24, 1997) ("BT/MCI Merger Order"). No such claim is remotely plausible here given that the combined entity will offer access services only in areas where competing facilities already exist and will provide less than five percent of such services even in areas where TCG has its greatest local presence.

Even beyond this dispositive fact, the vertical concerns expressed by Sprint and BellSouth are misguided. Sprint's sudden fear of vertical integration is deeply ironic given its own much more substantial vertical integration. Sprint also has the economics wrong. By substantially increasing TCG's financial strength (and hence its opportunities to deploy alternative access facilities) the merger will increase, not decrease, exchange access competition. Sprint's exclusionary conduct theory also ignores the fact that the combined entity's predominant business for the foreseeable future will continue to be long distance, and thus it will continue to be in the

combined entity's economic interest to place direct and indirect pressure on access rates wherever possible. In all events, as the Commission has recognized, the section 208 complaint process is more than adequate to address any claims of unreasonably discriminatory practices by AT&T/TCG or any other competitive LEC.

BellSouth's vertical claim that the license transfer will undermine universal service by heightening competition in the provision of exchange access services is spurious. Section 254 contemplates an explicit universal service subsidy mechanism and the end of the implicit (and bloated) access charge "subsidies" that BellSouth seeks to protect. And what BellSouth labels competitive "harm," is, in fact, an important public interest benefit of the merger. By providing TCG with more capital to invest in local facilities, the AT&T/TCG combination will increase access alternatives and pressure on BOC access prices. In short, the vertical integration of AT&T and TCG can only benefit competition and consumers and poses no threat of competitive harms.

Finally, a few commenters allege "redlining," "slamming" and similar issues that are wholly unrelated to the proposed transfer of control. As the Commission has stated, such allegations are beyond the scope of transfer of control proceedings and should be raised, if at all, by the filing of a complaint or, where appropriate, through a petition for rulemaking. In all events, the allegations are patently false.

ARGUMENT

Allegations of merger-related competitive harm are analyzed under the familiar framework of determining relevant markets, identifying significant market participants, reviewing the effects of the proposed transaction on the market power of the participants, and considering the potential for anticompetitive actions. See, e.g., Bell Atlantic/NYNEX Merger Order at ¶ 37.¹ The Commission then applies the same framework in determining whether the merger will produce efficiencies or otherwise enhance competition. Bell Atlantic/NYNEX Merger Order ¶ 37. An application seeking Commission consent to transfer control of licenses is approved so long as any demonstrated harms “are outweighed by benefits that enhance competition.” Id. ¶ 2. As demonstrated below, the integration of AT&T and TCG will have no adverse effects on competition in any market and promises enormous pro-competitive benefits in currently monopolized local markets. Accordingly, under the Bell Atlantic/NYNEX framework (or any other), the Application should be approved forthwith.

I. THE LICENSE TRANSFER WILL HAVE NO ADVERSE HORIZONTAL EFFECTS.

The proposed merger between AT&T and TCG “is predominately one between firms in a vertical relationship (i.e., they predominately interact through the supply of inputs to each other as opposed to through competing for customers).” BT/MCI Merger Order ¶ 206. AT&T provides long distance services and TCG makes local network facilities available for call origination and termination. By and large, the two companies simply do not today compete against one another

¹ See also United States Dep't. of Justice & Federal Trade Comm'n, *1992 Horizontal Merger Guidelines*, 57 Fed. Reg. 41552, 41554-41555 §§ 1.0 - 1.2 (1992).

for the same customers. And even where slight overlaps exist, the market share of one or both entities is so small, that no conceivable market concentration or competitive issue is raised. Indeed, the horizontal aspects of the AT&T/TCG combination are so insignificant that the commenters' allegations rest not on analysis of the relevant markets but only on references to potential overlaps. However viewed, these allegations are baseless.

Long Distance Services. BellSouth (at 9) concludes that "allowing AT&T to acquire the long distance business controlled by Teleport poses real risks to consumers of long distance service." But BellSouth does not and could not identify what those "risks" might be, for there are none. Indeed, this is presumably one of the reasons the proposed transaction has cleared a review by the United States Department of Justice without even a second request.

The long distance market is a national market,² and the continued vigorous competitiveness of the long distance business is one of the few givens in a telecommunications industry that is evolving at a dizzying pace. The Commission recognized in 1995 that no single firm could dominate the long distance business (at least so long as line-of-business restrictions properly limit BOC long distance authority). See Order, Motion of AT&T Corp. to be Reclassified as a Non-dominant Carrier, 11 FCC Rcd. 3271 (1995). The intervening three years have overwhelmingly confirmed the accuracy of that finding. The Commission's latest long distance report recognizes no fewer than 621 long distance competitors as of December 1996, nearly forty more than existed only one year earlier. Trends in Telephone Service, Industry

² See, e.g., Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Areas and Policy and Rules Concerning the Interstate, Interexchange Marketplace, CC Docket Nos. 96-149 et al. at ¶ 56 (FCC, released April 18, 1997).

Analysis Division, Common Carrier Bureau at 40 (FCC February 1998). AT&T's market share has continued to decline, pushing AT&T's share of revenues below fifty percent. Id. at 52. And long distance prices too continue to decline. See Merrill Lynch, Long Distance In-depth Report (March 4, 1998) at 1 ("long distance price pressures more than doubled in '97 -- the average rate per minute . . . fell 6.5% versus 2.2% in 1996"). As one group of analysts has noted, these statistics "evidenced one single thing: that the long distance industry, especially the mass market residential and single-line business markets, had very low barriers to entry. New entrants continue to take market share away from AT&T, MCI and Sprint." Id. at 6.

In these circumstances -- hundreds of existing competitors and low barriers to additional entry -- BellSouth would have a tough row to hoe in establishing significant competitive harm from any merger of long distance companies. But the claim is simply ludicrous in the case of AT&T's acquisition of TCG's modest long distance business.

TCG's long distance activities consist of its own internal interLATA efforts, and those of ACC Corp., which TCG recently acquired.³ TCG's own interLATA long distance initiatives are of very recent origin,⁴ have a very limited focus, and for the year 1997 produced revenues so small as to be inconsequential.⁵ ACC's long distance activities are also modest. The FCC's most

³ TCG closed on its previously announced acquisition of ACC Corp. on April 22, 1998. See TCG Press Release, found at <http://www.tcg.com/tcg/media/PRcurrent/accclose.html>.

⁴ TCG announced its plans to offer long distance services on September 15, 1997. See TCG Press Release: "TCG Bundles Long Distance Service for its Local Telephone Customers to Satisfy Demand for All Service/All Distance Carrier." The release noted that the offering will initially be made available to TCG's local telephone service customers, and that it was TCG's "first step" into the long distance market. This press release can be found at <http://www.tcg.com/tcg/media/PRarchives/ldroll.html>.

⁵ For the year 1997, TCG's revenues from interLATA long distance services were approximately \$6 million as compared to the tens of billions of dollars of industry revenues.

recent report states that ACC had \$118 million in 1996 long distance revenues, representing about one tenth of one percent of the \$82 billion total of 1996 interexchange carrier long distance revenues.⁶ ACC's 1997 United States revenues totaled only \$120.6 million, so its 1997 market share would be no greater.⁷ Under these circumstances, the license transfer will have no statistically significant impact on AT&T's market share or the level of "concentration" in the long distance industry.

That this is not a serious claim is confirmed by the fact that the "remedy" BellSouth proposes is that the Commission's approval of the pending AT&T/TCG applications be conditioned on "broad scale" BOC long distance entry. See BellSouth at 9-10. Congress did not authorize BOC entry into long distance -- through imposition of a condition on the grant of an application filed by a competitor, or on anything else -- unless and until the requirements of Section 271 have been satisfied. And the Commission has twice properly found that BellSouth has not met these requirements.⁸ Thus, it is plain that BellSouth's "horizontal" concern is a

⁶ See Table 3.2, Long Distance Market Shares Report, Industry Analysis Division, Common Carrier Bureau, March 1998.

⁷ See ACC Corp. Proxy Statement, March 27, 1998, at page 111. By its own description, ACC "operate[s] primarily as a switch-based reseller[]" and is only a part of "[t]he remainder of the U.S. long distance market . . . comprised of several hundred smaller companies, including ACC U.S., known as third-tier carriers." ACC Corp. Proxy Statement for Special Meeting of Shareholders at 95-96 (March 27, 1998). See also Bell Atlantic/NYNEX Merger Order ¶ 84 (third tier carriers "generally lack the brand reputation and recognition in the relevant markets that are critical assets for offering services to the mass market").

⁸ See Memorandum Op. & Order, In the Matter of Application by BellSouth Corp. to Provide In-region, InterLATA Services In Louisiana, FCC 98-17, 1998 WL 42491 ¶ 1 (rel. Feb. 4, 1998); Memorandum Op. & Order, In the Matter of Application by BellSouth Corp. to Provide In-region, InterLATA Services In South Carolina, FCC 97-418, 13 FCC Rcd 539 ¶¶ 12, 15 (rel. Dec. 24, 1997).

pretext and that BellSouth once “[a]gain[] would have the Commission serve that company’s own narrow interest rather than the broader public interest.” SBC Communications v. FCC, 56 F.3d 1484, 1493 (D.C. Cir. 1995).

Local Exchange And Exchange Access Services. The commenters’ allegations concerning the potential horizontal power of the merging parties in local markets consist of little more than passing references to TCG’s position as the largest alternative exchange access provider. Whether viewed from a national perspective, a state perspective, or even a metropolitan area perspective,⁹ however, it is clear that the combined AT&T/TCG exchange access presence will remain extremely limited. As Sprint points out, “the BOCs control virtually all of the access market.” Indeed, AT&T/TCG will not even “dominate” the single digit share not controlled by the BOCs -- Sprint, GTE and other non-BOC incumbents will remain much larger providers.¹⁰

Beginning at a national level, the FCC’s public data reveals that local telecommunications revenues for the year 1996 (the most recent period available) totaled \$96.5 billion.¹¹ TCG’s 1996 revenues of \$267.7 million¹² represented less than three-tenths of one percent of the national total

⁹ See BA/NYNEX Merger Order at ¶ 51 (“We will treat local exchange and exchange access services as a relevant product market separate from interstate, interexchange, long distance service”).

¹⁰ The Commission lists the major incumbent local exchange carriers and their respective financial information in its annual Statistics of Common Carriers publication. A list of CLECs can be found in New Paradigm Resources Group, Inc. Research Report on Competitive Telecommunications, Volume 6, No. 3, March 1998.

¹¹ See Telecommunications Industry Revenues: TRS Fund Worksheet Data, November 1997, FCC Industry Analysis Division, Figure 1 (total of local exchange, local private line, other local, and interstate and intrastate access service).

¹² See TCG’s Securities and Exchange Commission Form 10-K at page 27.

of \$96.5 billion. Even using TCG's higher 1997 revenues of \$494.3 million against this 1996 base would increase TCG's relative share to only about one-half of one percent of the total national local revenues.¹³ AT&T has publicly reported that its total 1997 local revenues from resale, use of unbundled elements, and its own facilities were only \$68 million.¹⁴ Adding this to TCG's 1997 revenues increases the total to only \$562.3 million, or slightly less than six tenths of one percent of the incumbents' total 1996 revenues, an insignificant market share by any measure.¹⁵

The story does not change if one reviews the impact of this proposed combination on an individual state basis. TCG's largest state market by far is New York. The dominant provider in New York is, of course, Bell Atlantic-New York. In addition, there are a number of independent incumbent local exchange carriers, including Frontier, and several other competitive local exchange carriers. FCC reports indicate that total revenues of New York local exchange carriers

¹³ Of course, the 1997 industry figures will be larger than the 1996 base, and so these figures, while modest by any measure, actually overstate TCG's national market share.

¹⁴ See AT&T First Quarter Earnings Report, Supplemental Disclosure IV. The \$68 million figure includes AT&T's Advanced Digital Link® ("ADL") revenues for that period. AT&T currently offers ADL as an outbound local calling service in 49 states and as an outbound and inbound service in New York, Connecticut, New Jersey, and California. See AT&T Earnings Commentary, April 20, 1998, First Quarter 1998 Summary.

¹⁵ It is important to note that a significant portion of AT&T's local revenues are composed of resold incumbent services, the underlying revenues from which are already counted in the incumbent's revenues.

for 1996 were \$8.4 billion.¹⁶ Bell Atlantic-New York, standing alone, accounted for at least \$7.0 billion of that figure.¹⁷

By contrast, although 35% of TCG's national revenues are derived from the greater New York metropolitan area (TCG's only presence in the state of New York),¹⁸ that corresponds to total revenues in New York state of only approximately \$94 million in 1996 and \$173 million in 1997. Measured against the total of \$8.4 billion, TCG's 1996 and 1997 revenues represent approximately 1.1% and 2.1%, respectively, of total New York State 1996 revenues. Even if one adds AT&T's entire \$68 million in nationwide local revenue to TCG's 1997 New York state revenues, the combination would still represent only 2.9% of total New York State 1996 local revenues.

Nor does looking at the New York City metropolitan area alone have any material effect on the analysis. Bell Atlantic-New York is again the dominant provider. Additionally, Bell Atlantic-New York has reported that about 25 companies resell Bell Atlantic-New York's services,¹⁹ functioning more as sales agents for Bell Atlantic-New York than as real competitors

¹⁶ See Statistics of Communications Common Carriers, Table 2.13 -- Revenues of Reporting Local Exchange Carriers for the Year Ended 12/31/96 (<http://www.fcc.gov/ccb/stats>).

¹⁷ See Statistics of Communications Common Carriers, Table 2.9 -- Statistics of Reporting Local Exchange Carriers as of December 31, 1996 and for the Year Then Ended, Column 18 (<http://www.fcc.gov/ccb/stats>).

¹⁸ Simon Flannery, J.P. Morgan Securities - Equity Research, Teleport Communications Group: Teleport Gave Upbeat Presentation of JPM High Yield Conference; Trimming Estimates, September 5, 1997.

¹⁹ Affidavit of Jacob J. Goldberg on Behalf of Bell Atlantic- New York, Petition of New York Telephone Company for Approval of its Statement of Generally Available Terms and Conditions Pursuant to Section 252 of the Telecommunications Act of 1996; and Draft Filing of Petition for InterLATA Entry Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-
(continued . . .)

to it. According to Bell Atlantic-New York, an additional three companies -- TCG, Cablevision and MFS/Worldcom -- operate alternative fiber networks in the New York City metropolitan area.²⁰

Bell Atlantic-New York has stated that approximately 80% of its New York State business revenues, and approximately 70% of its residential population, are located in the New York City metropolitan area.²¹ Assuming from this statement that 70% to 80% of Bell Atlantic-New York's revenues are derived from the New York City metropolitan area, that region would have produced between \$4.9 and \$5.6 billion of Bell Atlantic-New York's \$7.0 billion in 1996 New York State revenues. Even using the smaller number, TCG's 1996 and 1997 revenues (noted above) were only 1.9% and 3.5%, respectively, of that metropolitan area market. And, again, even the addition of all of AT&T's 1997 national local revenues (only a fraction of which actually came from New York City) to TCG's New York metropolitan area revenues would raise the 1997 TCG/AT&T share to only 4.9%. Thus, the combination of AT&T and TCG would produce at most a single digit HHI increase under any scenario.²²

(. . . continued)

Region, InterLATA Services in the State of New York, Case No. 97-C-0271, State of New York Public Service Commission, November 4, 1997, at 5 ("Goldberg Affidavit").

²⁰ Goldberg Affidavit at Map 2. Applicants do not believe that independent incumbent local exchange carriers serve any meaningful portion of this metropolitan area.

²¹ Goldberg Affidavit at 4.

²² Assuming that the local market had a single incumbent provider (with a 95.1% share) and that AT&T and TCG were the only other suppliers (in fact there are many others) the proposed merger would increase the HHI by only 9.8 -- from 9058.22 and 9068.02.

Although shares this small would not raise competitive concerns in any context, they are particularly insignificant here given that the local market strategies of TCG and AT&T have been quite different, that any overlaps are insignificant, and that incumbent LECs continue to enjoy enormous competitive advantages. TCG has focused almost exclusively on serving the local telecommunications needs of business users and residential customers in multiple dwelling units, using its own network and switching facilities. By contrast, AT&T has elected to offer services in seven states through the resale of incumbent LEC services.²³ Although AT&T has attracted 400,000 resale customers through those efforts, it (like others) has curtailed active marketing of resold services because incumbent prices and operational issues have made these services uneconomic.²⁴ AT&T's only facilities-based local networks are a modest "beta test" network in the Chicago area that serves a limited number of customers and AT&T's "Digital Link©" service (which uses AT&T's existing 4E switch network and requires that customers connect to that network through dedicated access and have their own premise equipment such as a PBX).²⁵

²³ AT&T offered resold local service to consumers in Alaska, California, Connecticut, Georgia, Illinois, Michigan, Texas and Rochester, New York. See AT&T Form 10-K, filed March 27, 1998.

²⁴ See AT&T Form 10-K, ("AT&T [has] stopped actively marketing resold local service to residential and small business customers in most of the areas in which it offered such service") MCI and Sprint have similarly abandoned active marketing of resold local services for the same reasons; see MCI Press Release, January 22, 1998 ("as long as the current regulatory environment continues, MCI will not offer resale service to any new residential customers"); Communications Daily, October 15, 1997 (reporting that Sprint has suspended advertising and marketing of resold services until economics can support mass marketing).

²⁵ See AT&T's Fourth Quarter 1997 Earnings Commentary, which can be found at <http://www.att.com/ir/commentary/974q-cmnt.html>.

The merger accordingly portends no conceivable adverse consequences to local competition. That is particularly so given the extreme levels of market power possessed by the BOC and other incumbent participants in local markets. As the Commission recently found, incumbents like BellSouth and Sprint "possess[] unique advantages not possessed by other market participants." Bell Atlantic/NYNEX Merger Order ¶ 107. Indeed, BellSouth's suggestion that the Commission should be concerned that AT&T is acquiring the largest "alternative" access provider is a bit like Microsoft complaining about another computer company acquiring the most popular personal computer operating system alternative to Windows.

International Services And 38 GHz Licenses. The commenters make only footnote references to potential horizontal overlaps with respect to the services actually provided pursuant to TCG's 38GHz and international licenses -- the licenses at issue in the applications pending in this proceeding. There are no horizontal concerns. With respect to international services, AT&T and TCG/ACC are only two of hundreds of carriers that provide such services, including MCI, Sprint, WorldCom, Cable & Wireless, Inc. and countless foreign carriers. The Commission declared AT&T nondominant with respect to the relevant international services more than two years ago.²⁶ TCG has virtually no long distance traffic (including international),²⁷ and ACC provides international service primarily through resale and has a truly de minimus international presence -- approximately \$2 million in international billed revenue in 1996, or less than two one-

²⁶ Order, Motion of AT&T Corp. to be Declared Non-Dominant for International Service, 12 F.C.C. Rcd. 17963 (1996). The four international markets in which the Commission found that AT&T is the sole facilities-based provider (Madagascar, Western Sahara, Chagos Archipelago, and Wallis and Futuna, id. ¶ 94) are not impacted by the AT&T/TCG combination.

²⁷ See, supra, note 4.

hundreds of one percent (0.014%) of the total international billed revenue for the largest 47 international carriers that year.²⁸ On these facts, there could be no credible claim that the merger presents horizontal concerns in any country-to-country international services market or the “global seamless service market.” See BT/MCI Merger Order at ¶¶ 128-131.²⁹

The same is true of the relevant 38 GHz licenses. There is no separate 38 GHz “market.” TCG’s subsidiary BizTel, which has links operating in virtually all of its licensed areas, uses its 38 GHz licenses as a microwave substitute for fiber interoffice transport in its provision of local exchange and exchange access services. As demonstrated above, the merger presents no competition concerns with respect to local markets. And even if some separate wireless market were appropriately considered here, it plainly would have to include cellular, PCS and other wireless licensees, not simply 38 GHz licensees, and the combined AT&T/TCG 38 GHz licenses would, by any measure, represent an insignificant portion of wireless traffic.

Additionally, no issue is presented by the fact that AT&T will, by virtue of this acquisition, now have two 38 GHz licenses in a few markets.³⁰ The Commission has not prohibited a single licensee from holding multiple 38 GHz licenses in a single serving area.³¹ Indeed, the Commission

²⁸ Trends in Telephone Service at 24.

²⁹ Further, neither of the merging parties has market power in any input market, and thus there could be no vertical claim here that the merger would allow AT&T/TCG to raise rivals’ costs, engage in a predatory price squeeze, or gain market power in end-user markets. Compare BT/MCI Merger Order at ¶¶ 163-204.

³⁰ AT&T and TCG have overlapping 38 GHz licenses in just 11 cities and only one of those, Augusta, Maine (population 21,325), will not be served by multiple 38 GHz licensees following the merger. AT&T’s ninety 38 GHz licenses tend to be located in rural areas, whereas TCG/BizTel’s 200-plus licenses are generally centered in more urban areas.

³¹ TCG/BizTel, for example, was granted two licenses in the New York metropolitan area.

has permitted 38 GHz licenses to acquire multiple licenses in a single market area by application, as well as through acquisitions and mergers; Winstar, to name only one example, has acquired multiple licenses in single service areas in this manner.

In sum, the merger will have no significant adverse horizontal effects in any market.

II. THE LICENSE TRANSFER WILL HAVE NO ADVERSE VERTICAL EFFECTS.

As the Commission has long recognized, “[v]ertical effects that harm competition generally depend on the vertically integrated firm possessing market power in an upstream ‘input’ market.” *Id.* ¶ 154 (emphasis added). That is because it is such market power that would allow the combined firm to “harm consumers through increases in prices, decreases in quality, or a reduction in alternatives in end-user markets.” *Id.* As explained above, there can be no serious claim that TCG’s limited alternative access facilities give it market power in “upstream” local exchange or exchange access markets. Rather, it is only BellSouth and its incumbent brethren that possess such market power. That should be the end of the matter with respect to the potential adverse vertical effects analysis.

But even if it were theoretically possible to identify legitimate vertical concerns in the context of a merger in which neither of the merging parties nor the combined entity will have market power in any market, Sprint and BellSouth have plainly failed to do so here. Sprint (at 3) speculates that the merger “may perhaps, in the long run” provide “AT&T with alternatives to BOC access services which AT&T may then deny its competitors.” Sprint’s claim is deeply ironic given that Sprint itself already enjoys the same vertical integration it challenges here -- only on a much larger scale. In all events, Sprint’s speculation ignores several key facts.

As an initial matter, AT&T/TCG will remain subject to the Section 201 and Section 202 prohibitions against unreasonable practices and unreasonable discrimination, as well as the Section 251(a) and Section 251(b) interconnection and dialing parity requirements. More fundamentally, following the merger, AT&T will remain predominantly a long distance carrier. It will continue to desire access to local networks and exchange access facilities around the country on favorable terms and it will continue to have every incentive to increase pressure on access charges, AT&T's single highest long distance input cost. With \$45 billion in long distance revenue compared to only \$500 million in local revenues, it will remain in AT&T's best interest for the foreseeable future to continue applying downward pressure on access rates.

Moreover, it is difficult to imagine how the merged companies could profitably employ the strategy posited by Sprint. Sprint ignores that TCG does not control any bottleneck exchange access facilities. All of TCG's local facilities are subject to direct competition from one or more incumbent local exchange carriers, competitive access providers, and competitive local exchange carriers. If TCG attempted to limit its customers' long distance choices, it would not only forego access revenues on the terminating end, but also lose end-user customers to competing access providers that did not limit customer choice in that manner on the originating end. AT&T could not hope to make up these losses in the long distance market, because in every case its long distance competitors could make alternative access arrangements.³² In fact, because TCG provides no more than four percent of exchange access services in any area, AT&T's long

³² The same cannot be said, of course, of most customers served by incumbents such as Sprint and BellSouth, both of which continue to be the sole access providers to many locations.

distance competitors would rarely have to make any alternative arrangements at all, and thus the strategy could not possibly impact long distance prices.

In short, Applicants will have strong economic incentives to encourage maximum utilization of their network facilities, in order to have as large a market as possible from which to recover their operating costs. Indeed, because AT&T's and Sprint's incentives with respect to access are largely aligned, the proposed merger should, if anything, enhance Sprint's access to competitive access facilities by increasing TCG's financial resources and allowing it to build more such facilities.

In all events, if at some point in the future AT&T engages in any practice that Sprint believes is unreasonably discriminatory (or otherwise unlawful), it can ask the Commission to investigate that practice and, if appropriate, devise a remedy, in the context of a section 208 complaint. It is precisely that authority that has led the Commission recently to reject similar across-the-board restrictions on competitive access providers. See First Report & Order, In the Matter of Access Charge Reform FCC 97-158 ¶ 363 (rel. May 16, 1997) ("Access Charge Reform Order") ("if an access provider's service offerings violate section 201 or section 202 of the Act, we can address the issue . . . through the exercise of our authority to investigate and adjudicate complaints under section 208").³³

³³ Sprint (at 5) also suggests that the Commission condition its approval of the proposed transfer of control on structural separation of TCG and AT&T. This suggestion should be rejected out of hand. The Commission has never required such structural separation with respect to a nondominant carrier because the inefficiencies of this practice can only be justified when there are serious anticompetitive concerns. Memorandum Op. and Order, In re Applications of Craig O. McCaw and AT&T Co. for Consent to the Transfer of Control of McCaw Cellular Communications, FCC 94-238 ¶ 124 (rel. Sept. 19, 1994) ("AT&T/McCaw Merger Order") ("We agree with AT&T and McCaw that to impose such requirements on the AT&T/McCaw entity would frustrate a customer's ability to meet all of its telecommunications needs through
(continued . . .)

Nor can any credence be attached to Sprint's concerns that there will be a "shortage" of competitive access providers.³⁴ Sprint executives stated this month that they will be announcing shortly their plans to launch local operations in markets served by other incumbent LECs. Certainly if Sprint believed the rhetoric of its comments -- that local market opportunities are diminishing -- Sprint executives would not be placing Sprint investment capital there.³⁵

BellSouth takes the opposite tack, complaining that the vertical integration of AT&T and TCG is likely to increase exchange access competition. That increased competition, BellSouth alleges, will harm residential customers by "siphoning off universal service funds" because of the savings in access expenses that will result. BellSouth at 7-8. BellSouth's premise is true -- the merger is likely to increase exchange access competition. But BellSouth fails to acknowledge the obvious: as the Commission has found, increased access competition and reductions in wildly inflated access expenses are public interest benefits, not detriments.³⁶ Thus, BellSouth once again

(... continued)

integrated service offerings from a single vendor, one of the notable benefits of the merger to the consumer. For these reasons, we decline to require structural separation or to prohibit joint marketing of cellular and long distance services") (footnote omitted); *id.* ¶ 125 ("The conditions warranting structural separation are not present here. AT&T is neither a monopoly wireline carrier nor a monopoly supplier of cellular service equipment, and the cellular equipment and equipment maintenance markets are competitive. We previously have declined to apply the structural separations rules in situations where competition rendered their application unnecessary").

³⁴ Sprint at 3-4.

³⁵ See Telecommunications Reports, April 20, 1998 ("Sprint: MCI-WorldCom Deal May Spark Internet Consolidation").

³⁶ Access Charge Reform Order ¶ 44; see also Report & Order, Federal-State Joint Board on Universal Service, FCC 97-157 ¶ 6 (rel. May 8, 1997).

“do[es] little more than complain that the merger . . . will lead to greater competition” and confuse the maintenance of its monopoly with the public interest.³⁷

Nor could those benefits pose any threat to universal service. BellSouth ignores the requirements of Section 254 of the Telecommunications Act of 1996, which establishes a new universal service mechanism based on efficient and explicit subsidies and not on excessive access rates. Under this system, any legitimate subsidies contained in interstate and intrastate access fees will be replaced with an explicit and competitively neutral collection mechanism, and all qualifying local carriers -- not just incumbents like BellSouth -- will be entitled to receive universal service subsidies from that explicit fund.³⁸ Moreover, under the Commission’s rules, universal service contributions are collected from all carriers, so that if a dollar of local revenue shifts from an incumbent to a competitive provider (or the reverse) the contribution to the universal service fund will be unchanged -- the support obligation follows the revenues.³⁹ Strengthened access competition therefore cannot undermine universal service, but will merely frustrate BellSouth’s apparent hope of both maintaining the current regime of inflated access charges and collecting the new explicit universal service subsidies at the same time. Thus, as has previously been the case, BellSouth graphically “fail[s] to show in any way why the merger would not be in the public interest,” and “more nearly show[s] the opposite.”⁴⁰

³⁷ See SBC Communications, Inc. v. FCC, 56 F.3d 1484, 1497 (D.C. Cir. 1995).

³⁸ Report & Order, Federal-State Joint Board on Universal Service, FCC 97-157 ¶ 6 (released May 8, 1997) (“In this proceeding, we modify the funding methods for the existing federal universal service support mechanisms so that such support is not generated, as at present, entirely through charges imposed on long distance carriers”).

³⁹ See 47 C.F.R. § 54.703.

⁴⁰ See SBC Communications, Inc. v. FCC, 56 F.3d 1484, 1497 (D.C. Cir. 1995).

III. THE AT&T/TCG MERGER WILL STRENGTHEN COMPETITION IN LOCAL MARKETS FOR BOTH RESIDENTIAL AND BUSINESS SERVICES.

Against this backdrop of no competitive harms, the enormous benefits of combining AT&T and TCG loom especially large. Not a single commenter disputes the existence of those benefits, which are detailed in the applications, and they are indisputable -- the combined entity unquestionably will be a more formidable local competitor in battling entrenched incumbent monopolists than either AT&T or TCG could be alone. Moreover, the Commission has recognized the formidable obstacles that face a new local competitor -- obstacles that this merger will directly address -- and thus the Commission's own experiences confirm the accuracy and genuineness of the benefits cited by AT&T and TCG.⁴¹

BellSouth nonetheless claims that these conceded benefits are inadequate in two respects. Both claims misapprehend the facts and the law. BellSouth first contends that the applications are wanting because the merger will benefit only business, and not residential customers. As the Application makes clear, however, residential customers will receive both immediate and long-term benefits from the merger. AT&T and TCG explicitly identified a set of residential customers that will be served immediately by the merged entity -- customers that live in "multiple dwelling

⁴¹ See Bell Atlantic/NYNEX Merger Order ¶ 42 ("Even upon hypothetical full implementation of the Telecommunications Act of 1996, significant barriers to entry into the local telecommunications marketplace will remain. Entrants must still be able to attract capital, as well as to amass and retain the technical, operational, financial and marketing skills necessary to operate as a telecommunications provider in the local market. For mass market services, entrants will have to invest in establishing the brand name recognition and, even more importantly, the mass market reputation for providing high quality telecommunications services. These consumer 'goodwill' assets take significant amounts of time and resources to acquire. An unknown entrant's attempts to build 'goodwill' by providing reliable, high quality service relies heavily on the cooperation of the incumbent LEC that provides interconnection, unbundled elements, resold services or transport and termination, and can be frustrated by the incumbent LEC if that carrier engages in discriminatory conduct affecting service quality, reliability or timeliness").

units in high density markets[.]” AT&T/TCG Application for Approval at 8. The merger also will “strengthen[] [AT&T’s] position as an entrant” in all local market segments and thus the long-term benefits of this merger will reach a much broader segment of the residential market. BT/MCI Merger Order ¶ 15.

The synergies of these two companies in providing a broader range of services are obvious and undisputed. AT&T will learn from TCG’s decade of providing local and exchange access services just as AT&T “gain[ed] valuable knowledge of how to provide cellular service to end-users” through its merger with McCaw Cellular Communications. AT&T/McCaw Merger Order ¶ 59. And TCG will benefit from AT&T’s brand name and unsurpassed experience in long distance markets. Cf. id. ¶ 57 (“The merger will allow McCaw to use AT&T’s strong brand name and its marketing and sales force”). TCG’s ability to expand its services to smaller businesses and residential consumers has been limited by the lack of a recognized market identity, which the merger will instantly cure. The vertical integration of these companies will further “result in . . . cost reductions, productivity enhancements, [and] improved incentives for innovation,” “support the general policies of opening markets and lowering entry barriers that underlie the 1996 Act,” BT/MCI Merger Order ¶ 41, and enable the combined entity to provide bundled local and long distance services to a greater array of residential and business customers. See Memorandum Op. and Order, In re Application of Pacific Telesis Group and SBC Communications for Consent to Transfer Control of Pacific Telesis Group and its Subsidiaries, FCC 97-28, ¶ 48 (rel. Jan. 31, 1997) (“SBC/Pacific Merger Order”) (“[o]ne-stop shopping is a benefit arising from increased competition”). And AT&T, whose experiences with resold services have been discouraging to say the least, will have an “alternative local infrastructure . . . within its control and management,”

Application at 7, rather than having to rely on the begrudging “cooperation” of entrenched incumbent monopolists.

But even if, contrary to the fact, BellSouth were correct that the merger would strengthen competition in the business services market segment only, that would provide no basis to disapprove the license transfers. To enhance competition in even one segment of local services markets would be a substantial benefit for the public. Because the merger concededly will benefit business customers and could have no adverse effect on competition in providing services to residential customers, the proposed transfer of control patently advances the public interest. Bell Atlantic/NYNEX Merger Order ¶ 2.

BellSouth next suggests that the substantial competitive benefits detailed in the applications should be ignored because the applications themselves are too short. But, as the Commission has made clear, the “public interest standard is a broad, flexible standard[],” and “[d]ifferent cases will present different facts and competitive circumstances.” Bell Atlantic/NYNEX Merger Order ¶ 2, 12. There is accordingly no “minimum” page requirement for public interest statements, particularly where, as here, the relevant competitive benefits are so self-evident that no party -- including BellSouth -- disputes them. Even more fundamentally, BellSouth simply ignores that the Commission’s public interest standard contemplates a balancing of competitive benefits against potential harms. As demonstrated above, the vertical integration of AT&T and TCG will cause no competitive harm in any market. In these circumstances, the Commission has consistently recognized -- both before and after the Bell Atlantic/NYNEX Merger Order -- that an application that makes only the slightest claim of competitive benefits